**TENNESSEE DEPARTMENT OF REVENUE**
**LETTER RULING # 00-14**

**WARNING**

**Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.**

## SUBJECT

Application of the Tennessee sales and use tax to crates used by the taxpayer for the delivery of milk to its customers.

## SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the department by the taxpayer. The rulings herein are binding upon the Department and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time.

Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

> (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
> (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
> (C) The applicable law must not have been changed or amended;
> (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
> (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

## FACTS

[TAXPAYER] is engaged in the dairy processing business with a facility located in [CITY], Tennessee. The taxpayer processes fluid milk, dairy related products, and fruit juice products (hereinafter all products will be referred to as "milk") at its [CITY], Tennessee facility. The taxpayer sells the milk, primarily for resale, but does make some direct sales to users and consumers.

The taxpayer purchases milk crates which are delivered to the [CITY] production facility. The taxpayer delivers its milk products to its customer's locations in the milk crates. The milk is packaged in other containers (e.g., cartons) before it is placed in the crates. Depending on the arrangement with the particular customer, the taxpayer's route delivery person may unpack the crate at the customer's location or (usually with respect to the larger customers) the crates may be left on the customer's dock for unpacking by the customer's employees. The crates are ultimately returned to the taxpayer. The taxpayer does not make a separate charge to its customers for the crates. The taxpayer states that the delivery of the product is impractical without the use of the crates.

## QUESTION

Are the crates that the taxpayer uses in the delivery of its milk products subject to the Tennessee sales or use tax?

## RULING

The taxpayer's purchase of the crates is subject to sales tax. In the event that sales tax is not paid on the purchase of the crates, the taxpayer would owe use tax on them.

## ANALYSIS

Tenn. Code Ann. § 67-6-102(24)(E) states, in pertinent part:

> "Sale at retail," "use," "storage," and "consumption" do not include the sale, use, storage or consumption of:
>
> * * *
>
> (ii) Materials, containers, labels, sacks, bags or bottles used for packaging tangible personal property when such property is either sold therein directly to the consumer or when such use is incidental to the sale of such property for resale ...

Tenn. Code Ann. § 67-6-102(24) operates to negate in part other provisions of the Retailers' Sales Tax Act that would otherwise impose sales or use taxes. Therefore, the rules of statutory construction that apply to exemptions apply to the construction and application of Tenn. Code Ann. § 67-6-102(24). *See*, *Hutton v. Johnson*, 956 S.W.2d 484 (Tenn. 1997). Tax exemption statutes are to be construed against the taxpayer and exemptions will not be implied. *Hyatt v. Taylor*, 788 S.W.2d 554 (Tenn. 1990). Every presumption is against exemption, and any well founded doubt defeats a claimed exemption. *United Canners, Inc. v. King*, 696 S.W.2d 525 (Tenn. 1985). The burden is upon the taxpayer to establish a claimed exemption. *Woods v. General Oils, Inc.*, 558 S.W.2d 433 (Tenn. 1977).

TENN. COMP. R. & REGS. 1320-5-1-.11 (hereinafter "Rule 11" or "the Rule"), entitled "Containers, Wrapping and Packing Materials and Related Products" interprets Tenn. Code Ann. § 67-6-102(24). The first paragraph of the regulation states:

> Items actually accompanying the product sold or shipped, without which the delivery of the product is impracticable on account of the character of the contents, and for which there is no separate charge, are not subject to Sales or Use Tax. These items include such things as containers, packing materials, labels or name plate affixed to products manufactured, and printed matter containing only directions for use.

The Rule must be read in conjunction with the statute. While the Commissioner of Revenue is authorized to prescribe reasonable rules and regulations not inconsistent with the taxing statutes under Tenn. Code Ann. § 67-1-102, such rules and regulations may not enlarge the scope of either a taxing statute or an exemption. See, *Covington Pike Toyota, Inc. v. Cardwell*, 829 S.W.2d 132, 135 (Tenn. 1992); *Volunteer Val-Pak v. Celauro*, 767 S.W.2d 635, 637 (Tenn. 1989); *Coca-Cola Bottling Co. v. Woods*, 620 S.W.2d 473, 475-76 (Tenn. 1981).

In *Coca-Cola Bottling Co. of West Tennessee v. Celauro*, 1993 WL 330303 (Tenn. 1993), the Tennessee Supreme Court considered the exclusion from sales tax for containers found in the statute. In that case, Coca-Cola used pressurized tanks to deliver either a "pre-mix" or "post-mix" soft drink syrup. Pre-mix tanks contained a solution of syrup, water, and carbon dioxide that could be dispensed directly into a drinking container for the consumer. Post-mix tanks contained only soft drink syrup so that the customer was required to combine the syrup with water and carbon dioxide before the product was served. Coca-Cola's customers consisted primarily of restaurants which sold soft drinks directly to consumers. The pressurized tanks were delivered to the restaurants, or other customers, and connected to a dispensing unit. Empty tanks were either returned by the customer or retrieved by Coca-Cola and were cleaned and used again. No separate charge was made to the customer for the tank.

In construing the statute, the Court determined that the product tanks used by Coca-Cola were incidental to the sale of the soft drink products for resale. The evidence showed that there was no practical alternative for the product to be sold "to customers for resale without use of the product tank." The Court did not discuss Rule 11 in this case, but the Court's ruling is consistent with the Rule's requirement that delivery of the product would be impracticable without the container.

In *Evans v. Memphis Dairy Exchange*, 194 Tenn. 317, 250 S.W.2d 547 (1952), the Court considered a predecessor to the current statute. At that time, the exemption provided:

> The terms 'sale at retail,' 'use,' 'storage,' and 'consumption' shall not include the sale, use, storage or consumption of industrial materials for * * * nor * * * materials, containers, labels, sacks or bags used for packaging tangible personal property for shipment or sale.

In that case, Memphis Dairy Exchange sold bottles to distributors who used the bottles in packaging milk for delivery to consumers. Consumers paid the distributors a deposit of three cents per bottle in order to assure the return of the bottle to the distributor. The Court held that the sale of the milk bottles to the distributors was not a taxable sale at retail under the above statute.

In the *Coca-Cola v. Celauro* and the *Memphis Dairy Exchange* cases cited above, the packaging at issue consisted of the packaging which immediately held the actual property to be sold, a liquid, that is, tanks to contain soft drinks or bottles to contain milk. Further, the product remained in the packaging at issue until after the product was delivered to the vendor's immediate customer. In the taxpayer's case, the crate is a second container which does not accompany the milk to the end consumer, and, in a significant number of cases, does not accompany the milk into the hands of the taxpayer's immediate customer. While it is not suggested that a second container holding the container in which the product is immediately contained would always be considered taxable, here, the second container is mainly for purpose of expediting delivery than to hold the product. Due to that main purpose, its exemption is not contemplated by the statute.

Further, the Attorney General opined, in Opinion No. 83-459, 1983 Tenn. AG LEXIS 35 (October 26, 1983), on the taxability of crates which appear analogous to the crates at issue in this ruling. After quoting the statue and the rule, the Attorney General used the following analysis to conclude the crates were subject to tax:

> The regulation would cover packaging materials accompanying the product to the consumer. The statute itself appears to be somewhat ambiguous. Prior to the amendment of Chapter 149 of the 1971 Public Acts, T.C.A. § 67-3002(c)(2) [now T.C.A. § 67-6-102(24)(E)(ii)] excluded from the definition of "sale at retail," "use," "storage," and "consumption" "materials, containers, labels, sacks or bags used for packaging tangible personal property for shipment or sale." The 1971 amendment appears to have qualified the exemption. Under the present statute, containers used for packaging tangible personal property would only be exempt when either the tangible personal property is sold in the container directly to the consumer, or when the use of the container is incidental to the sale of the tangible personal property for resale.
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> As a general rule, tax exemption provisions are most strongly construed against the person claiming exemptions. *Crown Enterprises, Inc. v. Woods*, 557 S.W.2d 491 (Tenn. 1977); *Hall Contracting Corp. v. Tidwell*, 507 S.W.2d 697 (Tenn. 1974).
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> When the proper application of a statute is not entirely clear, the first inquiry is to ascertain the general legislative intent. State by *Lockert v. Knott*, 631 S.W.2d 124 (Tenn. 1982); *Tidwell v. Collins*, 522 S.W.2d 674 (Tenn. 1975); *Worrall v. Kroger Co.*, 545 S.W.2d 736 (Tenn. 1977). Once an ambiguity exists as to the interpretation of a statute, it is appropriate to turn to the legislative history of the statute for guidance. *Chapman v. Sullivan County*, 608 S.W.2d 580 (Tenn. 1980).

> A review of the legislative deliberations on May 4, 1971, in regard to House Bill 509, which became Chapter 149 of the 1971 Public Acts, shows the following intent of the Act as noted by Senator Ayres:
> House Bill 509 "clarifies the present law with respect to the exemption from taxation of packaging and packaging material under the Retail Sales Tax Act. The Bill provides that packaging materials are exempt only when used in connection with the sale of personal property. The effect of this is to remove the exemption when packaging material is used solely for purposes of shipment without any attempt to sell a part of the container therein... In other words, if the packaging material is involved in the transportation or shipment of goods - these would not be exempt from the imposition of the Retail Sales Tax."
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> Therefore, it would appear that the clear legislative intent of the 1971 amendment was to impose a tax upon containers and packaging materials which do not accompany the item sold to the consumer. This would likewise be true of all packaging and shipping items that are not passed along to the consumer in the sale.

While this opinion was rendered before *Coca-Cola v. Celauro*, supra, the tanks in *Coca-Cola* clearly remained with the product until after the sale to Coca-Cola's immediate customer. The facts in *Coca-Cola* are distinguishable from those on which the Attorney General Opinion was rendered.

In light of the analysis above, the crates are not within the exemption for packaging and are subject to the sales or use tax. The taxpayer will be liable for tax on its purchase of the crates.

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APPROVED: Ruth E. Johnson
Commissioner

DATE: 5/15/00